

2 U.S. UNITED STATES DEPARTMENT OF AGRICULTURE  
Rural Electrification Administration "

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A Statement on  
REA GENERATION & TRANSMISSION LOANS  
And How They Help Farmers "

The fundamental objective of the REA program is to help the farmers of America to get electric power in the most reliable manner at the lowest possible cost. In many cases, due to power shortages in rural areas or exorbitant rates charged by commercial utilities, this can be done only if farmers have the right and the means to build their own generating and transmission systems.

In the Rural Electrification Act of 1936, the Congress specifically gave REA the authority to make loans for the construction of rural generating and transmission systems. Section 4 of the Act states: "The Administrator is authorized and empowered, from the sums hereinbefore authorized, to make loans...for the purpose of financing the construction and operation of generating plants, electric transmission and distribution lines or systems for the furnishing of electric energy to persons in rural areas..."

REA policies for making this type of loan have been developed in accordance with the law and the expressions of the Congress. The policy regarding generation and transmission loans was established during the first few months of REA by its first Administrator. It was discussed by Senator Norris on the floor of the Senate in the debate on passage of the Rural Electrification Act in 1936. It has been discussed many times in the Congress since then. It is written in REA's book on policy, as follows:

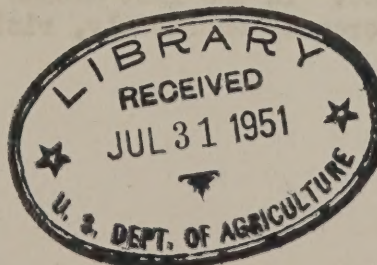
"The Rural Electification Administration will make loans to finance the initial construction of generation facilities and transmission facilities only under the following conditions:

- "a. Where no adequate and dependable source of power is available in the area to meet the borrower's needs, or
- "b. Where the rates offered by existing power sources would result in a higher cost of power to the borrowers than the cost from facilities financed by REA."

That REA has conscientiously adhered to this policy over the years is indicated by the following facts:

First, the Congress and committees of the Congress from time to time during the last 15 years have carefully investigated REA's operations under the

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"G&T" policy as well as specific loans made under that policy. Each time the Congress has decided to continue the provision of the Act unchanged in any way. Perhaps the most detailed of these inquiries was that made in 1950 by the Agriculture Subcommittee of the House Committee on Appropriations and Subcommittees of the Senate Committee on Appropriations, as well as on the floor of the Senate. The discussions were concluded with the following report by the House and Senate conferees on the 1951 appropriation: "...the Rural Electrification Administration is expected to exercise its power generation authority only in line with its announced policy and the law."

Second, a much greater number of applications for G&T loans fail to receive approval than are approved because the proposed facilities do not meet the requirements set forth in the REA policy. Applications from co-op federations in Ohio, Illinois, Florida, Pennsylvania and Mississippi are recent illustrations of applications that were not approved because it appeared that the cooperatives were able to obtain adequate quantities of dependable and low-cost power from existing sources.

It should be emphasized that these applications for loans were entirely proper and could have been approved under the provisions of the Rural Electrification Act. They met the requirements of the law, but they did not meet the requirements of REA policy, which is more strict than the law.

As a reading of the REA G&T policy will reveal, the loans for G&T serve two major purposes: they enable farmers to get adequate and reliable power, and they give farmers a means for assuring themselves more reasonable rates. Let us examine these two points, taking first the matter of power supply and second power cost.

Power Supply. The rural demand for power has increased tremendously because of the huge number of farms electrified since World War II and because of unprecedented expansion in the use of electricity by the individual farmers. As a result of this increase in consumers and in use per consumer, the total amount of electric energy distributed by REA borrowers rose from about 300,000,000 kwh in fiscal 1940 to more than 6,000,000,000 kwh in fiscal 1950--- a 20-fold increase in 10 years. Estimates made by REA and its borrowers on the basis of existing trends and other known factors indicate a likely billing of 20 billion kwh or more by REA borrowers for the year 1960 -- more than 3 times the amount billed in 1950 -- provided that adequate power at reasonable rates is available where and when needed during the intervening years.

This growth of co-op power demands has caused and will continue to cause a terrific power supply problem. The co-ops have turned to every possible means to solve it.

One source is the commercial power companies. The rural electric co-ops and other REA borrowers are substantial customers for the power companies as the following table indicates. In the last decade the purchases from commercial power companies have increased enormously, rising from 211,136,327 kilowatt hours



in 1940 to 4,059,218,990 kilowatt hours in 1950. The volume of this business for the power companies has increased from 2 $\frac{1}{2}$  million dollars in 1940 to 37 $\frac{1}{2}$  million dollars in 1950.

Electric Power Purchased by REA Borrowers  
From Commercial Power Companies

<u>Year</u>	<u>Kilowatt Hours Purchased</u>	<u>Amount Paid</u>	<u>Year</u>	<u>Kilowatt Hours Purchased</u>	<u>Amount Paid</u>
1940	211,136,327	\$ 2,608,347	1946	1,217,847,475	\$11,996,403
1941	358,758,065	4,209,588	1947	1,697,760,828	16,456,650
1942	537,608,251	5,744,296	1948	2,354,502,542	22,685,610
1943	668,405,812	7,002,203	1949	3,191,543,216	30,681,759
1944	814,285,256	8,521,913	1950*	4,059,218,990	37,634,987
1945	979,110,684	9,894,762			

\* Preliminary figures subject to revision.

Despite the large amounts of power purchased from the commercial power companies, the requirements for additional power of the rural electric systems have been even larger and they have had a serious problem in finding an adequate supply.

What has been making the situation even more difficult for many REA borrowers has been the failure of the utility industry as a whole to anticipate adequately the postwar surge of demand for more and more power. With generating capacity utilized to the limit, many power companies in all sections of the country found themselves unable to meet even the demands of their regular urban and industrial customers, and the rural electric co-ops often had to bear the brunt of such power shortages.

In a few cases, this situation has been recognized and acknowledged by the companies themselves. This was the case in North Dakota, where the Otter Tail Power Company, noting that the co-ops already were taking a quarter of all the electricity the company was providing in that region, frankly stated its inability to provide the additional amount the co-ops were going to need immediately and in the near future. Such admissions have been the exception; most companies have maintained in public a pretense of their ability to meet any and all demands, in spite of long records of increasingly poor service and letters to individual co-ops refusing to provide additional amounts of power.

In order to meet their growing power needs, the rural electric systems have been forced in many cases to supply themselves with power either by generating it themselves or by building facilities that would enable them to obtain power from public projects.

The following table indicates how the loans for generation and transmission facilities have increased as the program has grown:



REA Loans by Fiscal Years, G&T and Total Loans

<u>Fiscal Year</u>	<u>Total Loans</u>	<u>G&amp;T Loans</u>	<u>G&amp;T Loans as Percent of Total</u>
1936	\$ 13,903,412	\$ 28,000	0.2
1937	45,032,805	1,482,000	3.3
1938	29,236,219	1,154,000	3.9
1939	139,064,513	3,484,000	2.5
1940	41,736,000	568,000	1.4
1941	100,054,672	5,612,150	5.6
1942	91,152,724	28,162,700	30.9
1943	6,700,978	1,695,294	25.3
1944	31,930,124	3,017,550	9.5
1945	25,731,055	5,719,924	22.2
1946	289,372,488	31,920,043	11.0
1947	254,521,172	33,329,895	13.1
1948	313,023,099	39,978,033	12.8
1949	448,859,597	85,000,526	18.9
1950	375,151,456	136,439,210	36.4

As has been indicated, this increase is accounted for not by any change in REA policy but by these facts: (a) The enormous growth of co-op power requirements, (b) the inability or unwillingness of many existing suppliers to acknowledge the growing co-op needs and help the co-ops take care of them, and (c) the need that the co-ops have for gaining access to low-cost public power for which, under the law, they are preferential customers.

The extent of the power supply problem the borrowers are up against is further indicated by the fact that of the applications for loans now on hand almost 60 percent, or \$230,000,000, are requests to finance generating plants and transmission lines.

Power Cost. The fact that farmers are able (through REA loans) to build their own generating and transmission systems has had an effect on the cost of electric power to the farmer in two ways: (1) through the bargaining power provided, and (2) through actual generation or through transmission of low-cost power from public projects.

The effectiveness of this bargaining power is indicated by the reductions in wholesale rates the REA borrowers have been able to obtain on power purchased from commercial utilities. For example, while the average wholesale cost per kwh purchased by REA borrowers from commercial power companies nation-wide decreased from 10.1 mills in 1945 to 9.6 mills in 1949, in the New England States and New York area (where G&T loans in the past have not proved feasible) the rate increased from 12.1 mills in 1945 to 13.5 mills in 1949.

Here is another example of what the bargaining power means. During the calendar year 1949, a total of 211 distribution-type REA borrowers purchasing power from commercial companies were benefited by rate reductions obtained that year as a result of G&T loans requested but not made. The annual savings to these 211 REA borrowers, based on the present volume of their power consumption, amount to \$1,339,452, compared with what they would have had to pay under the old rates. Based on expected power consumption after their line construction program under existing distribution loans has been completed, the annual savings are estimated to be about \$2,700,000.



The effect on rates, of course, of G&T loans approved as well as those not approved, goes far beyond the immediate area concerned. All farmers have benefited indirectly from the threat of competition in the power field.

The bonafide rate reductions referred to above should not be confused with "propaganda" offers which have of late been proposed to a number of cooperatives which have received G&T loans. That such offers are made for propaganda purposes is evident from the following facts:

1. They come at a time when the farmers composing the co-op, having undertaken a variety of commitments, are extremely unlikely to accept them.
2. They are put forward in the full knowledge that REA, having entered into a loan contract with the co-op, has no legal or moral right to cancel the contract except with the consent of the co-op.
3. The rates proposed are often below those charged other customers of the power company and are thus subject to so-called "friendly" suits, leading to cancellation of the contract and increased rates once the threat of a co-op generation plant has been removed.

The rural power picture has had the prospect of being aided recently by the construction of several river development projects. Under the 1944 Flood Control Act, cooperatives are among those given preference for power produced by these projects. To rural people this preference is highly important. In the first place, low-cost power can mean the difference between electrification on a self-liquidating basis and no electricity at all. In the second place, low-cost power is essential if farmers are to make full use of electricity.

It is obvious, however, that this preference does the farmer no good unless he has the means for getting the power. Here again REA loans are providing farmers with means for exercising a right they have under the law.

The loan to the Old Dominion Electric Cooperative of Virginia illustrates this. In September, 1949, REA approved a loan of \$14,320,000 to the cooperative, a federation of distribution co-ops, to build a steam power plant and a network of transmission lines. The steam plant was needed to "firm up," as the engineers express it, the power soon to become available from the Federal dam across the Roanoke River at Buggs Island. The transmission lines would bring this public power, for which the co-ops are preference customers, to their load centers.

For several years the co-ops had been trying to get additional power and better service from the Virginia Electric and Power Company, the principal wholesale supplier in the area. The new power system also promised relief from the relatively high rates VEPCO charged them. But the company repeatedly refused to provide additional power, and the facilities from which the co-ops got wholesale service were inadequate for even their present needs. But almost coincidentally with our approval of the Old Dominion loan, the company effected an interchange agreement with another company under which VEPCO had access to additional power, and then it offered a very substantial rate reduction.



REA co-ops in Virginia are under jurisdiction of the State Corporation Commission. After extended hearings, that Commission in December, 1950 refused to permit Old Dominion to proceed with construction, apparently believing that this time VEPCO could and would live up to its promises. The co-ops which are members of Old Dominion indicated they might appeal to the courts from this Commission ruling.

A loan to the Central Electric Power Cooperative of South Carolina, also a federation, provides another illustration. That loan, for \$7,595,500, was approved in January, 1949. Here, too, the principal supplying company had a record of high prices, poor service, and inability or unwillingness to meet future co-op needs.

The State of South Carolina owns and operates a power dam harnessing the waters of the Santee and Cooper Rivers, and the Federal Government has two dams under construction on the Savannah River. Our loan was for the construction of transmission lines, which the State agency operating the Santee-Cooper Dam agreed to lease and operate. These lines would bring cheap public power from all these sources to the co-op load centers. Fifteen months after the loan was approved, the company suddenly offered a very substantial rate reduction and launched a bitter, extensive and expensive propaganda campaign containing misleading half-truths and outright false statements.

The rate reduction, bringing the price down almost exactly to that provided in the Santee-Cooper contract, was announced with the open statement that it was offered solely to stop construction of the new lines. It was the second reduction which the company had offered under pressure of a threat of co-op facilities, the other having been made in 1943 after REA approved a loan for generation and transmission facilities. War conditions precluded construction then.

The lines of Central are well along in construction now, and the campaign of opposition apparently was suddenly withdrawn when the announcement of the new Atomic Energy Commission facilities to be built in the area revealed the basic inadequacies of present power facilities there.

Other such loans have been made in Missouri, Oklahoma, Arkansas, the Dakotas, and other States.

These loans were made to enable the rural people to obtain directly the benefits of low-cost, hydroelectric power from public power projects in the area, through such agencies, for example, as the Southwestern Power Administration -- one of the public power marketing agencies of the Department of the Interior.

Because of the misunderstandings there are in regard to loans of this type, here is a brief outline of those made in the southwest.

Pursuant to these loans, REA is financing the construction of transmission and generation facilities of only such capacity as is required to meet the power needs of the electric distribution cooperatives which are members of the



federated cooperatives. Certain of the transmission facilities are leased to Southwestern Power Administration for the purpose of enabling SPA to deliver power to the member cooperatives' load centers pursuant to a power exchange contract between SPA and the federated cooperatives. The federated cooperatives expressly reserve for their own use the total capacity of the transmission facilities. During the period before the full rural load develops, certain of these transmission facilities may have temporary surplus capacity, which will be available to SPA for serving other consumers, but the federated cooperatives reserve the right to require SPA to surrender to the federated cooperatives the entire capacity of the transmission facilities whenever needed. SPA has the option of purchasing the transmission lines upon payment of the amount of the REA loan.

The question has been asked why such an option was given to SPA. The basic answer is that the farmers were thereby able to obtain a better over-all power contract.

The plan for a federated co-op to obtain an REA loan for construction of transmission lines whose ownership will eventually vest in someone other than the co-op was first worked out early in 1949 in a power contract between a federated co-op, the Dakotas Electric Cooperative, Bismarck, North Dakota, and a commercial power company, the Montana-Dakota Utilities.

The arrangement provides for the power company to maintain and operate the transmission line and to pay the co-op a monthly rental sufficient to amortize the REA loan over a 35-year period. Since the power company will, in effect, pay for the cost of the line anyhow, the co-op felt, and REA agreed, that the company should be given the right to obtain title to the line. The company may purchase the line at any time and is obligated to consummate the purchase when 40 percent of the principal of the REA loan has been repaid. By agreeing to transfer ownership of the transmission line to the power company, the co-op was able to obtain a more satisfactory power contract than would otherwise have been possible.

Essentially the same considerations, with one major exception, apply in the case of power contracts between federated co-ops and a public agency such as SPA. The exception is that the contracts with SPA provide merely for an option instead of for outright sale. The reason for this is that, whereas a private corporation such as a commercial power company can readily make a binding commitment, a public agency is subject to considerations beyond its control. The exercise by SPA of this option which is binding on the co-op but not on SPA will, of course, depend on whether SPA has, or will be given, specific authority by Congress to acquire the lines.

The generating facilities are not leased to SPA nor is any option given to purchase them. The federated cooperatives merely sell the output of the plants to SPA. With its hydroelectric power thus firmed up, SPA will be able to deliver to the member cooperatives power in quantities considerably greater than the capacity of the REA-financed generating plants. In addition to assuring the member cooperatives this firm block of power, SPA assumes the obligation of supplying the full needs of the cooperatives to the extent that



power is available. The arrangements thus effected will result in power cost savings to co-ops in Missouri and Oklahoma of more than 2 million dollars a year over existing power costs. In addition, in most instances, these arrangements will supplant the present inadequate sources of supply with an adequate and dependable supply of power.

Loans of this character are not unusual in the rural electrification program, nor are they confined to the public power field. Similar arrangements have been made with commercial power companies in North Dakota and Iowa. With ample supplies of lower-cost power, the cooperatives will be able to extend central-station electric service to thousands of unserved rural people and to serve their present consumers more adequately.

The G&T loans -- particularly those which give the farmers access to public power -- have been vigorously attacked by commercial power companies. In view of the savings farmers are able to make by having such loans, it is perhaps not surprising that there should be this opposition. Actually it boils down to a question of whether or not farmers have the right to supply themselves with power in the event such a course is to the farmers' advantage. The REA policy with respect to G&T loans as a matter of fact assures the commercial industry a preference in supplying the REA borrowers with wholesale power, because it is only after the co-op applicants show that (a) not enough power is available or (b) the loan would result in lower-cost power that a loan stands any chance of approval. Many farmers vehemently declare this policy unduly restricts their right to provide themselves with independent sources of power. They point out that no farmer cooperative in any field has been fully secure until it is able to control supply back to the source. This, of course, is the reason why many farm co-ops have found it necessary to own, for example, their own refineries and even their own oil wells, to have their own fertilizer plants, and to process their own feed supplies.

As long as electric cooperatives have the means through REA loans to exercise their right to generate or transmit power for their own use they will be able "to go back to the source" if they need to do so. The Congress, by expressing endorsement of the REA policy, indicates that G&T loans shall be used to help the farmers of America get electric power in the most reliable manner at the lowest possible cost. For REA to deviate from this policy -- either by refusing to make loans or by making those that do not meet the requirements -- would obviously be contrary to the will of the people as expressed through the Congress.